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ABSTRACT

In 1994, Michigan voters approved Proposal A, which reduced school property taxes, increased the sales tax, and established a per-pupil funding guarantee for public schools. This report describes the effects of Proposal A and challenges to it. Since Proposal A was implemented, funding for schools has grown substantially while property taxes have fallen, as promised. However, school districts have levied additional taxes, resulting in a millage-rate growth of over 60 percent in 6 years. Michigan legislators continue to explore ways to increase the taxing powers of local school districts beyond those allowed by Proposal A. One proposal would allow districts to use "sinking-fund" taxes to pay costs that go beyond their intended use. To better understand the impact of such legislation on taxpayers, this report simulated the effects of increased school sinking-fund taxes over a 10-year period and found a substantial tax increase. As a result, the report presents the following options for Michigan policymakers: (1) retain Proposal A; (2) consider regional taxes; (3) prohibit "double dipping"; (4) tighten allowable purposes for debt millage; (5) expand charter schools; and (6) insist on better management. (Contains nine charts and graphs, and photocopies of state documents itemizing Proposal A.) (WFA)

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Expanded School Sinking Fund Taxes

Infrastructure Investment, or Backtracking on Proposal A?

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Executive Summary

PROPOSAL A AND SCHOOL FINANCE

On March 15, 1994, Michigan voters approved "Proposal A," amending the Michigan Constitution to permanently reduce school property taxes, permanently increase the sales tax, and establish a per-pupil funding guarantee for public schools across the state. The tax limitation portion of the amendment requires a 3/4 supermajority vote in both chambers to pass laws that increase limits on the maximum amount of property taxes that may be levied for school district operating purposes.[1]

The statutory tax limits protected by the new provision of the Constitution were listed in a memorandum authored by deputy directors of the Budget and Treasury departments before the election, and distributed by the Governor shortly afterwards.[2] The memorandum lists specifically the sections of the school code that govern the allowable school operating taxes, including those that govern debt, sinking fund, and building & site taxes.

Very soon after Proposal A passed, there were attempts to increase the limits on operating taxes through an expansion of the use of these millages. Governor John Engler rebutted these attempts, stating in a veto message "we cannot stand by and let that historic step forward be reversed piecemeal by those that preferred the old school finance system--a system that was unfair to students and taxpayers alike."[3] However, before the end of the year 1994, the legislature did enact, and the governor signed, three laws that expanded the allowable school operating and debt millage.[4]

EFFECTS OF PROPOSAL A AND EXPANDED MILLAGE PURPOSES

Since Proposal A was implemented, funding for school districts has grown substantially. As shown by Figure 1, "Changes in Price, Enrollment, and Taxpayer Funding Since "Proposal A"," on page 5, and Figure 5, "School Operating Revenue vs. Enrollment," on page 7, these increases have occurred in an environment of low inflation and steady enrollment, so that real, per-pupil revenue for public schools has increased substantially since Proposal A was passed.

In keeping with the promise of Proposal A, local school district operating property taxes have fallen, with schools receiving increased revenue from the higher state

1. The ballot description language is included in "Appendix One: Proposal A Ballot Language" on page 24.
2. The March, 1994 memorandum to Governor John Engler was authored by Patrick L. Anderson, then deputy budget director; and Nick Khouri, then chief deputy treasurer. It is included in "Appendix Two: 1994 Memo on Statutory Tax Limits" on page 25.
3. The Governor's 1994 veto message, addressing SB 597 (1994), is included in "Appendix Three: 1994 Veto Message" on page 31.
4. PA 173 of 1994 allowed for certain districts to levy millage for swimming pools, and exclude that millage from their "operating millage;" PA 278 of 1994 amended section 1351a of the school code to expand the use of school debt millage; PA 258 of 1994 increased the allowable Intermediate School District millage. See Patrick L. Anderson, *The Tax Limits in Proposal A*, Michigan Chamber Foundation, January 1997.

sales tax, the new state property tax, and other sources.[5] Figure 2, "Local School Operating Taxes," on page 6, shows how local school operating taxes fell sharply in 1994, and the average millage rate for operating purposes has remained steady since then.

However, a growing segment of property taxes—indeed the fastest growing segment of property taxes—has been the various additional taxes levied by school districts such as debt, building & site, and sinking fund taxes. Since 1994—when Proposal A was passed, and a subsequent statutory expansion in the allowable purposes for debt millage was enacted—the revenues from these taxes have exploded. Figure 3, "Debt, Sinking Fund, and Building & Site Taxes," on page 6, shows how the average millage rate among Michigan Schools for these purposes has grown over 60% in just six years—from an average of 2.6 mills in 1994 to 4.1 mills in 2000. The tax revenue from such millages has grown 117%, to nearly a billion dollars in 2000.

RECENT LEGISLATIVE INITIATIVES

Michigan legislators are once again exploring ways to increase the taxing powers of local school districts beyond those allowed when Proposal A passed. Several bills have been introduced to allow school districts to levy taxes that will effectively increase operating revenues. House Bill 4824 has had the most success, passing the House in December, 2001. A similar bill, SB 688, was introduced in the Senate in October, 2001.

Both SB 688 and HB 4824 would allow districts to use "sinking fund" taxes to pay costs that go well beyond the proper use of a sinking fund, which is to repay the principal owed on a debt. Passage of such a law would effectively allow schools to increase their operating tax revenue, by using "sinking fund" revenue to cover repair, maintenance, refurbishing, "technology," and furnishing costs that would normally be paid out of operating funds.

Such a change in purpose is acknowledged in the bill by a provision allowing the tax to be described to voters using words other than "sinking fund," such as "infrastructure investment fund."[6] By authorizing 5 additional mills to be levied for such purposes, the legislature would effectively increase the maximum school property tax for operating purposes by 5 mills. For businesses and other taxpayers paying 18 mills in local taxes plus 6 mills in state taxes now, a 5-mill increase would represent more than a 20% tax increase.[7]

5. See "The Taxes Funding Michigan Schools" on page 8.

6. A particularly reckless provision would allow for *unspecified* descriptions of the tax to appear on the ballot. Such a provision would be a green light to experimenting with the language until the voters approve a ballot measure, thus fraying the connection between the actual uses of the funds and the description approved by the voters.

7. For homeowners exempt from the 18-mill operating tax levy, an additional five mills would nearly double their current six-mill state school property tax.

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In addition to these bills, there has been discussion of expanding the use of debt millage, building & site millage, and proposing a special state bond issue that would subsidize local expenditures.[8]

ASSESSING POTENTIAL FISCAL IMPACT

To better understand the impact of such legislation on taxpayers, we simulated the effects of increased school sinking fund tax authority over the next decade, under 3 scenarios.

Each scenario measures the potential impact of HB 4824 over the period 2003-2013, with 10% of the total tax increase occurring in each year. Our base scenario (Scenario One) assumes an average statewide increase of 2.5 mills on both real and personal property taking place over the ten years following passage of the bill. This is equivalent to half of the school districts levying the 5-mill tax by the end of the ten-year period.

This base scenario closely reflects the trend that occurred from the time at which the allowable debt millage purchase was liberalized, 1994, through the most recent year for which data is available, 2000. Over these 6 years the statewide average millage for debt, sinking fund, and building & site taxes increased .25 mills a year. Our base scenario of a 2.5 mill increase over 10 years assumes that, if the legislature liberalizes "sinking fund" millage as it did previously for debt millage, "sinking fund" taxes will grow at about the same rate over the following ten years as the debt millage category grew in the six years following the 1994 law changes.

Scenario Two is more conservative, assuming only a 1.5 mill average statewide increase; Scenario Three assumes a 3.5 mill increase. In each of these alternate scenarios, we also assume that the average millage increases 1/10 of the total change each year for ten years.

Table 1, "Summary of Sinking Fund Tax Impacts," below, shows the cumulative additional property taxes that would be levied by schools under each scenario over a ten-year period.

TABLE 1. Summary of Sinking Fund Tax Impacts

Scenario	Cumulative Property Tax Increase (billions)	*Residential Burden*	*Non-Residential Burden*
Base Scenario, 2.5 mill average increase	$5.43	*$3.37*	*$2.06*
Scenario Two, 1.5 mill average increase	$3.26	*$2.02*	*$1.24*
Scenario Three, 3.5 mill average increase	$7.60	*$4.71*	*$2.89*

Source: Anderson Economic Group

8. See "Recent Legislation" on page 12.

These projections are illustrated in Figure 4, "Property Tax Increases Under Different Scenarios," on page 7. As indicated in the table and figure, our base scenario results in a cumulative tax increase of over $5.4 billion. The low and high scenarios are for tax increases of $3.3 billion and $7.6 billion, respectively. About 5/8 of these tax increases would fall on residential property, and the remainder on non-residential property.

BACKTRACKING ON THE TAX LIMITATIONS OF "PROPOSAL A"

While the size of the fiscal impact may be surprising, the policy implications should not be. An overwhelming number of Michigan citizens adopted Proposal A, indicating their express agreement with a system that permanently limited school property taxes, and established a funding system that included a permanently higher sales tax rate. They have supported other taxes that have allowed school funding to grow significantly faster than inflation. To now adopt legislation that expands school property taxes—even if disguised somewhat in terminology—would strike many voters as reneging on that tax limitation commitment.

Given that there is no discussion of permanently reducing the sales tax or state property tax rates, many voters would be understandably angry with backtracking on the tax limits in Proposal A.

POLICY OPTIONS

In addition to the proposed tax increases, Michigan policymakers have a number of options. They include:

1. Retain the current law, noting that Proposal A was overwhelmingly approved, and has largely succeeded in its principal objectives of reducing school property taxes, increasing school funding, and reducing the disparity in per-pupil funding among school districts.
2. Prevent "double dipping" by allowing only one form of capital millage—either debt, sinking fund, *or* building & site—to be levied at any one time.
3. Encourage—or require—that sufficient operating funds be devoted to the maintenance of existing structures, so that local school districts would not find themselves in "crises" arising from unmaintained buildings.
4. Rely more on public school academies—also known as charter schools—that fund their capital expenditures out of the per-pupil operating funds. Charter schools could be especially helpful in areas with growing or declining enrollment. On the other hand, expanding the use of debt, building & site, and sinking fund millage as a source of operating funds would further aggravate the existing disparity in funding between public school academies and traditional public schools.
5. Use the regional taxing authority under current law, which provides for school districts to join together in asking voters to increase local taxes to augment spending for operating purposes. The law allows for up to 3 mills of taxing authority, on an intermediate school district-wide basis.
6. Tighten the statutes governing the allowable purposes for debt millage revenue, to once again prohibit the use of long-term borrowing to pay for short-term assets or operating expenditures. This would not only improve fiscal prudence, it would also increase the confidence with which voters view school bond issues.

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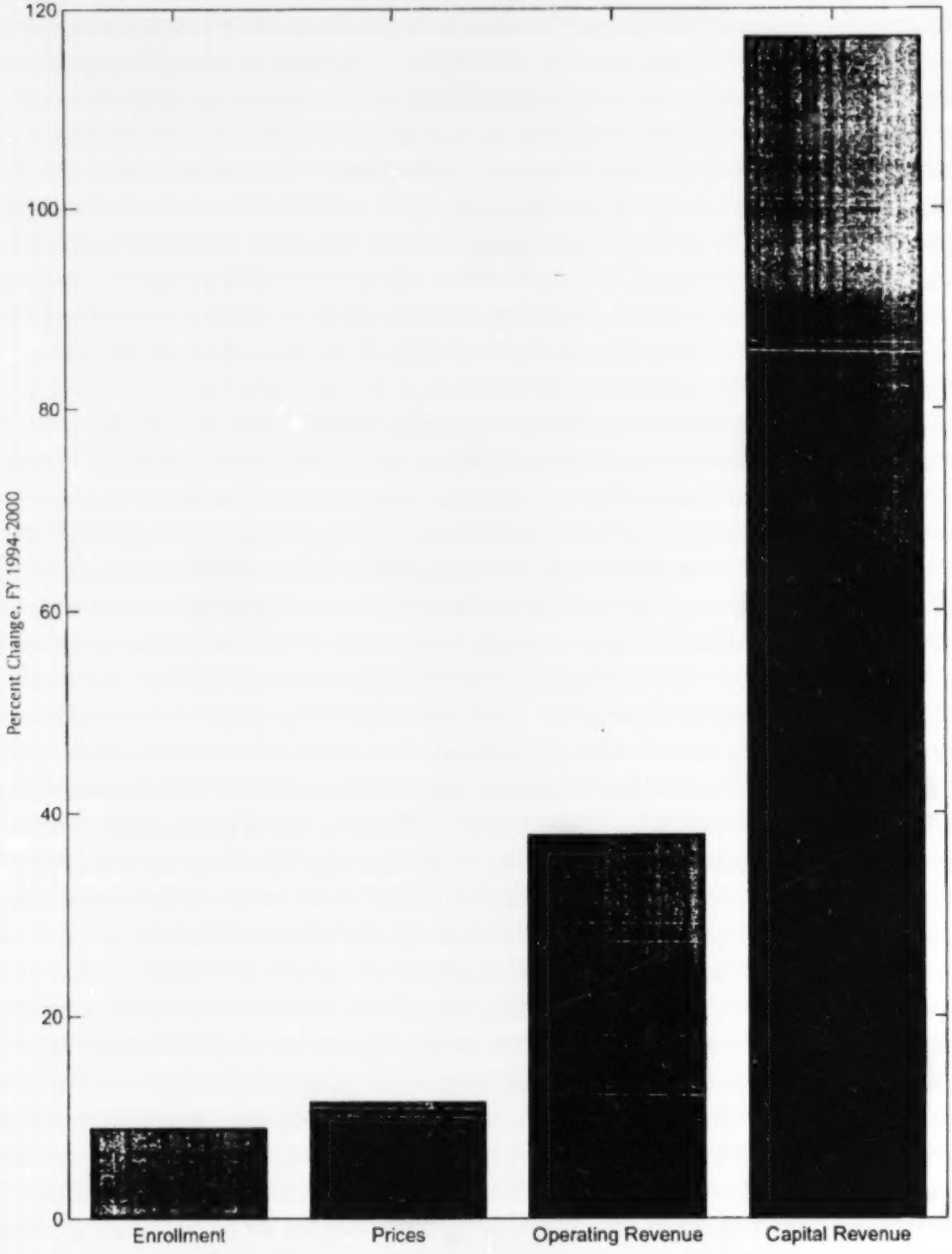
Figure 1. Change in Prices, Enrollment, and Taxpayer Funding since 'Proposal A'



Source: Anderson Economic Group

Data: Michigan Dept. of Education; Michigan State Tax Commission; BEA

page 5

Figure 2. Local School Operating Taxes

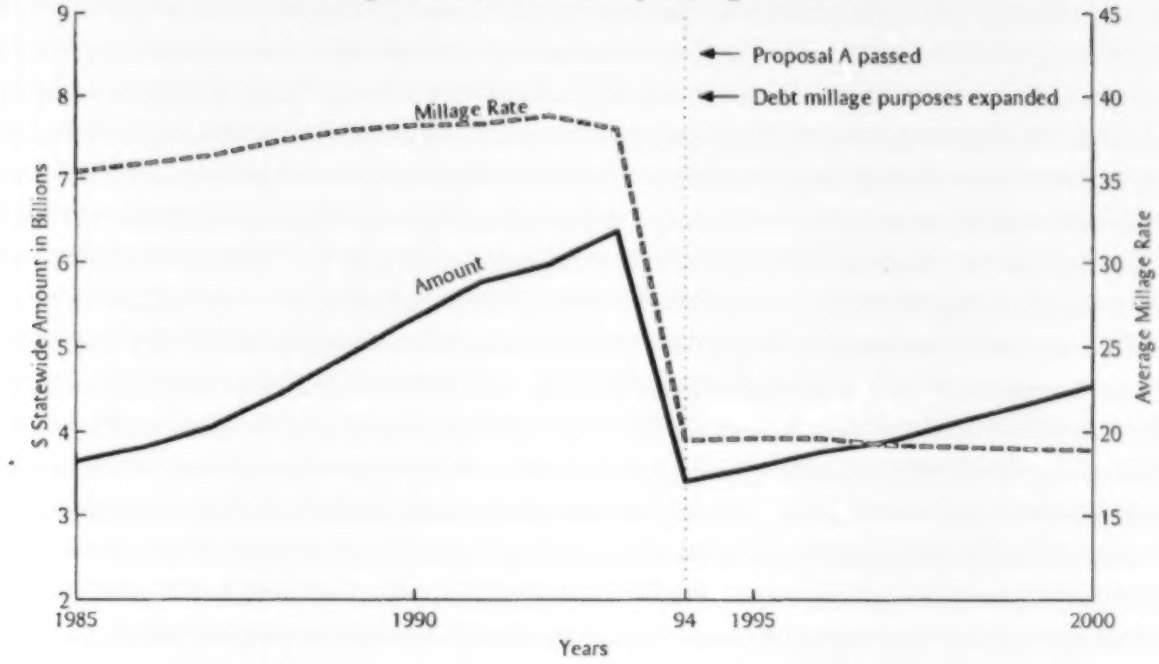
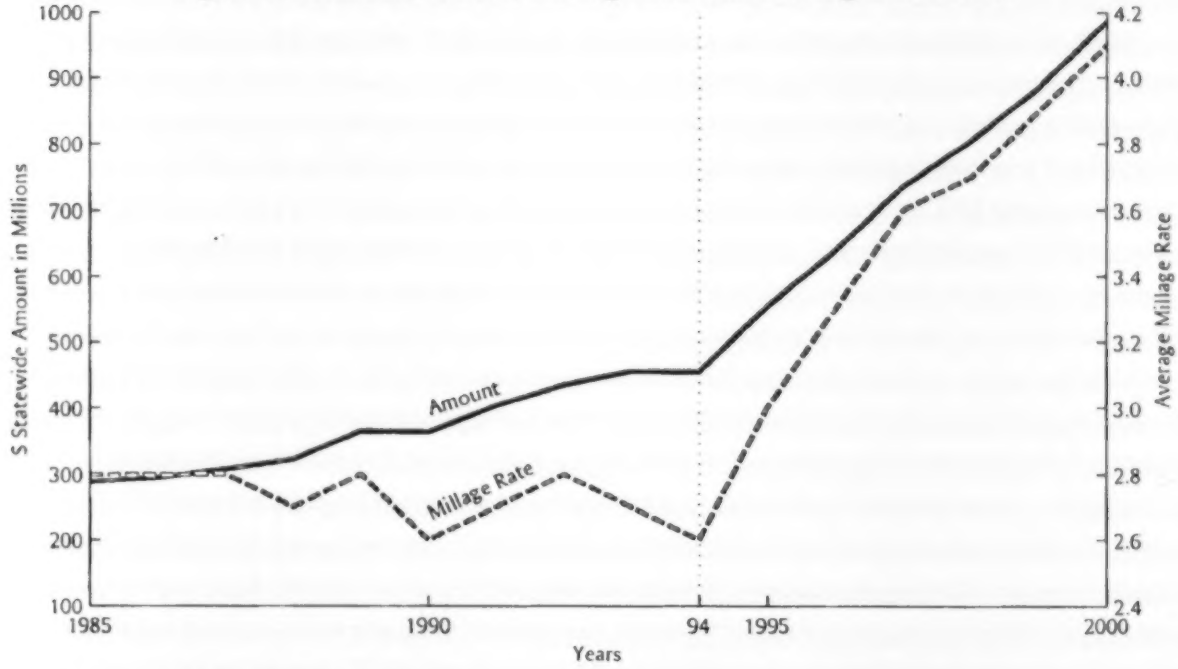


Figure 3. Local School Debt, Sinking Fund and Building & Site Taxes



Source: Anderson Economic Group
Data: Michigan State Tax Commission
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Figure 4. Property Tax Increases Under Different Scenarios

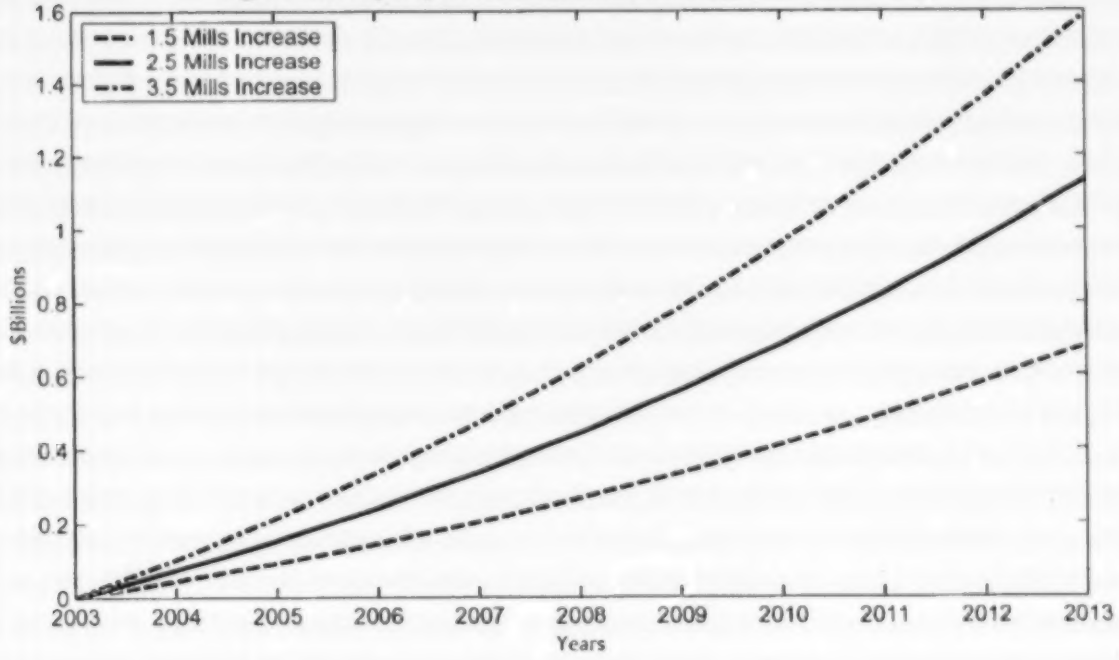
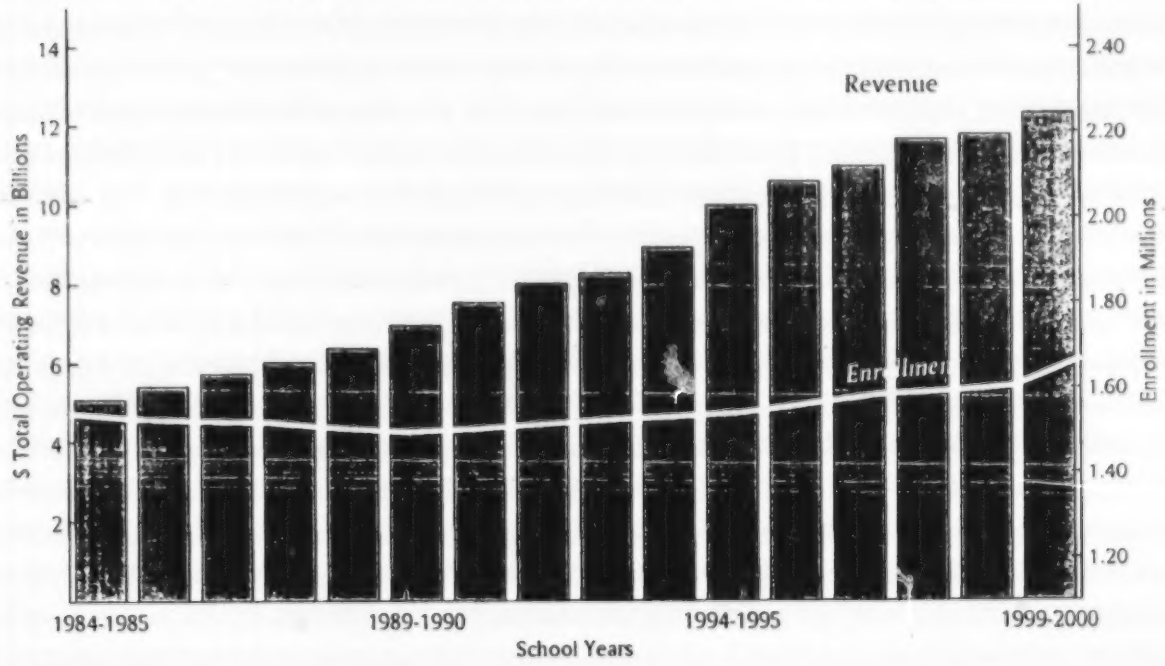


Figure 5. Statewide Local School Operating Revenue vs. Enrollment



Source: Anderson Economic Group
Data: Mich. Dept. of Education; Mich. Senate Fiscal Agency; Mich. Dept. of Treasury
Generated Date: 04/12/2002

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The Taxes Funding Michigan Schools

Public schools are currently financed by a set of taxes, including:

1. Local property taxes of approximately $4 billion, the majority of which is generated by an operating tax of about 18 mills levied by local school districts on non-homestead properties. Other local school taxes include hold-harmless taxes, building & site millages, sinking fund millages, and debt millages.
2. A state education property tax of 6 mills on all property, which generates approximately $1.4 billion.
3. The entire proceeds of the additional 2% sales tax added by Proposal A in 1994, plus a portion of the proceeds of the first 4% sales tax. Of the total sales tax revenue of approximately $6.5 billion, about three-quarters goes directly to the school aid fund.
4. Portions of the proceeds of other taxes, including the individual income tax, the tobacco tax, liquor excise tax, the real estate transfer tax, and the use tax.[9]
5. Additional taxes that support the K-12 system, including Intermediate School District operating millage, ISD debt millage, and Community College millage.

The Tax Limits Under Proposal A

Proposal A, adopted by the voters on March 15, 1994, amended Article IX section 3 to include the following sentence:

> A law that increases the statutory limits in effect as of February 1, 1994 on the maximum amount of ad valorem property taxes that may be levied for school district operating purposes requires the approval of 3/4 of the members elected to and serving in the Senate and in the House of Representatives.

The ballot language for Proposal A is included as "Appendix One: Proposal A Ballot Language" on page 24.

WHAT TAX LIMITS ARE PROTECTED?

The statutory limits that were protected by Proposal A were listed in a March 2, 1994 memo to Governor Engler by Patrick Anderson (then Deputy Budget Director) and Nick Khouri (then Chief Deputy Treasurer). The text of this memo is included as "Appendix Two: 1994 Memo on Statutory Tax Limits" on page 25. The memo was distributed before the election was held on March 15, 1994.

Listed explicitly in the memo are the various sections of the revised school code that govern operating and capital millage, including the debt, "sinking fund," and building & site millage authorizations.[10]

Following the affirmative vote of the electorate, the Governor sent the memorandum to the Secretary of the Senate, Clerk of the House, Speaker of the House, Sen-

9. For a useful summary, see *Annual Report of the State Treasurer*, various years, available from the Michigan Department of Treasury web site.

ate Majority Leader, and other officials, including the state board of education. In his transmittal letter, he stated "We are all obligated to uphold the wishes of the citizens, as expressed by their adoption of this constitutional amendment....The attached memorandum, summarizes these statutory limits."

THE 1994 VETO

The Governor did not need to wait long before the legislature tested both the 3/4 vote requirement, and the limits on millage levied for operating purposes. Senate Bill 597 was passed by the legislature in April, and allowed for an expansion of the use of building & site millage, the use of sinking funds for technology purposes, as well as an increase in the allowable purposes for bond funds. The bill was passed without a 3/4 vote.

The Governor returned the bill on April 14, 1994 without signature. In his veto message, he noted that his previous letter had transmitted a memorandum listing the protected tax limits under Proposal A, and that the sections of the school code that the bill would change were on that list. He also found the expanded uses of bond, sinking fund, and building & site millages were "fiscally imprudent" and not an "appropriate" use of these funds. Furthermore, wrote Engler:

> Proposal A promised Michigan homeowners permanent property tax relief--guaranteed in the Constitution. That promise cannot and will not be broken...
>
> We cannot stand by and let that historic step forward be reversed piecemeal by those that preferred the old school finance system--a system that was unfair to students and taxpayers alike.

The complete text of Engler's veto message is contained in "Appendix Three: 1994 Veto Message" on page 31

SUBSEQUENT CHANGES

The Michigan Chamber Foundation commissioned a review of the tax limits protected by Proposal A in late 1996. In *The Property Tax Limits in Proposal A, Are the Taxpayers Getting What They Bargained For?*, Patrick Anderson listed the bills that were adopted by the legislature that increased the tax limits protected by the 3/4 vote limit. As of the end of 1996, there were already 10 bills that had varied the limits. One, SB 597, was vetoed by the governor. One increased an exemption (thus reducing taxes), and did not require a 3/4 vote. The other eight were tax increases, received a 3/4 vote, and were signed by the governor. Two of these, PA 173 and PA 278 of 1994, expanded school borrowing powers.

The report lamented the fact that many of these votes were taken without the legislature knowing that a 3/4 vote was required, and that only one chamber had adopted rules requiring such a vote.

10. Patrick L. Anderson, Nick Khouri, Memorandum to Governor John Engler, Michigan Department of Management and Budget, March 2, 1994. The table and text in the memo list, along with other laws, sections 1211, 1211a, 1211c, 1212, 1351a, 1356, and 1451 of the revised school code governing operating, enhancement, debt, sinking fund, and building & site millage.

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LEGISLATIVE RULES

Both chambers of the legislature have now adopted rules that require the extraordinary vote for a change in the tax limits protected by Proposal A. House of Representatives Rule 55 requires a 3/4 vote on "Any law which increases the February 1, 1994, statutory limits on the maximum amount of ad valorem property taxes that may be levied for school district operating purposes. (See Const 1963, Art 9 § 3.)" Senate Rule 3.501 is similar.

Bond, Building & Site, and Sinking Fund Millage

The school aid act and revised school code establish funding for school operating purposes.[11] Since Proposal A, such funds have been explicitly allocated on a per-pupil basis. Proposal A further guaranteed minimum funding for every school district, again on an operating purposes, per-pupil basis.[12]

Bond, building & site, and sinking fund millages can be prudent vehicles to raise funds for capital projects. "Capital" projects are those that create long-term physical capital, such as buildings and land. Borrowing long-term to finance such capital can be prudent, much like a 30-year mortgage is a reasonable way for a family to buy a house. However, to allow them to be used as a supplement to operating millage is imprudent, if not reckless. Bonds that will take 20 years to repay should not be used to pay for services, nor for short-lived assets. Short-lived assets like school buses and "technology" have a useful life of three to seven years—imprudent expenditures for debts repaid over ten or twenty years.[13]

11. Article VIII of the 1963 Michigan Constitution, the education article, begins with the words of the 1787 Northwest Ordinance, based largely on a plan authored by Thomas Jefferson: "Religion, morality and knowledge being necessary to good government and the happiness of mankind, schools and the means of education shall forever be encouraged." The second section of the Article establishes the state legislature as the body responsible to "maintain and support a system of free public elementary and secondary schools as defined by law." The school aid act and school code are the two main laws that "maintain ... schools as defined by law."

12. Proposal A added these provisions to the end of Article IX, section 11, which also establishes the school aid fund and dedicates taxes to this fund. See also "The Taxes Funding Michigan Schools" on page 8.

13. The useful life of such expenditures can vary, but the Internal Revenue Code is a good guide. Sections 1245 and 1250 of the Code list cars, light and heavy duty general purpose trucks, qualified technology equipment, and computers and peripheral equipment as depreciable five-year property. See, e.g., *Master Tax Guide*, Chicago, Commerce Clearing House, various years; paragraph 1240.

The Internal Revenue Code tends to exaggerate the useful life of assets, as this approach increases tax collections. Many taxpayers expense immediately a good share of "technology" expenditures, noting that operating system and application software; computers and peripherals; and wiring, PDA's, telecom equipment and accessories are often obsolete within two to three years.

To ensure that operating funds are not commingled with funds intended to be used for separate purposes, the School Code requires that school districts create budgets for operating, building & site, and debt millage separately.[14]

BOND MILLAGE

The most well-known of the non-operating millages is debt millage. Since passage of the "Headlee" amendment in 1978, taxes can be levied above and beyond operating millage limits to pay for principal and interest on bonds, if they have been approved by the voters.[15] This requirement matches the state constitutional requirement that the voters approve state "general obligation" debt.

The voter-approval requirement forces school districts to make the case for debt millage. While there have been some end-runs around this requirement (notably the invention of "limited tax general obligation bonds,") this voter-approval requirement has been generally accepted.[16]

BUILDING & SITE MILLAGE

"Building & Site" millage was designed to allow segregated millage for the construction and major expenditures required by physical assets.[17] It is separate from operating millage.[18] However, to the extent that "building & site" millage pays for maintenance or other expenditures that should be paid from current revenues, it is actually a levy for operating purposes.

"SINKING FUND" MILLAGE

A sinking fund has a specific, technical meaning: it is a fund created and increased solely to repay principal on a debt.

An encyclopedia definition of the term is:

> [A] sum set apart periodically from the income of a government or a business and allowed to accumulate in order ultimately to pay off a debt. A preferred investment for a sinking fund is the purchase of the government's or firm's bonds that are to be paid off.[19]

---

14. Revised School Code, section 432; note that this section applies specifically to first-class districts.
15. Under Article IX section 6 of our Constitution, all property taxes are subject to a limit. The limits established by charter or general law for operating millage can be exceeded, provided the voters approve the levy of taxes to pay principal and interest on bonds. The limit for debt millage is established by the principal outstanding, rather than a rate.
16. For a discussion of the "limited tax" bonds, see the Anderson, et. al, *Report of the Blue Ribbon Commission on the Headlee Amendment*, Michigan Department of Treasury, 1994; also available at www.andersoneconomicgroup.com.
17. The Revised School Code, sections 622 and 1215, requires segregation of debt retirement and building & site millage proceeds from operating funds.
18. The General Property Tax Act, section 24e, defines "building and site" millage as distinct from operating millage and debt millage.
19. Found at www.encyclopedia.com. An identical entry is in *The Columbia Encyclopedia*, Sixth Edition. 2001, found at www.bartelby.com.

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The notion of a "sinking fund" is that money is accumulated over time (sinking), so that when a lump sum comes due on a loan, the accumulated funds will be available. Michigan has allowed school districts to levy "sinking fund" millages to build up funds to pay for future capital projects, much like bond sinking funds are used to pay for past projects.

Changes Since Proposal A

Since Proposal A passed in 1994, the following changes have occurred:[20]

1. School funding has grown dramatically, and the gap between the lowest-spending and highest-spending school districts has become much smaller. In 1994, over four-fifths of Michigan's school districts had less than $5,400 per pupil in operating revenue, and two-fifths had less than $4,500. By 2000, the *minimum* funding per student was $5,400, and a good number of districts had spending of $6,000 or more.[21]
2. The overall state-and-local tax burden, relative to other states, has become closer to the national average. Before Proposal A, Michigan had one of the highest property tax burdens in the country, and an overall tax burden that was significantly above the national average. Michigan's overall tax burdens are now slightly higher than the national average.
3. The number of millage elections has fallen, and the share of those millage proposals presented to voters that pass has risen.
4. As a feature of Proposal A, school operating millage has declined. However, school building & site, debt, and sinking fund millage has grown dramatically. From 1994 to 1997, annual tax revenue from these millages grew from $451.9 million to $723.9 million—a 60% increase in just three years. By 2000, the tax revenue from these millages had grown to nearly $1 billion—a 117% increase in tax revenue in just six years.[22] The average millage rate had grown during this short period from 2.6 mills to 4.1 mills. See Figure 1, "Changes in Price, Enrollment, and Taxpayer Funding Since "Proposal A"," on page 5.

Recent Legislation

HOUSE BILL 4824

House Bill No. 4824, introduced on May 24, 2001 and passing the House on December 13, 2001, calls for an amendment to the revised school code.[23] The bill would allow the levy of up to 5 mills on the taxable value of both real and personal

20. Unless noted, the source data for these observations is *Proposal A: A Retrospective*, Michigan Department of Treasury, August 1998.

21. *Economic Report of the Governor, 2000;* "School Finance Reform," page 62.

22. Tax revenue data from Michigan State Tax Commission. 2001 data were not available at the time of writing. See Figure 3, "Debt, Sinking Fund, and Building & Site Taxes," on page 6.

23. The bill would amend section 1212 of the Code.

property for up to twenty years. Currently, this section of the revised school code authorizes a tax levy for the purpose of establishing a sinking fund. However, under the bill revenue generated from the taxes could be used for any purpose allowed for debt millage.[24]

Such a change in law would greatly increase the scope of projects that school districts could fund with such taxes. Although "sinking funds" were originally intended only to pay for capital expenses, the bill would allow "sinking fund" taxes to fund:

- Purchasing, erecting, completing, remodeling, or equipping or re-equipping school buildings, including library buildings, structures, athletic fields, playgrounds, or other facilities, or parts of or additions to those facilities.
- Furnishing or refurnishing new or remodeled school buildings.
- Acquiring, preparing, developing, or improving sites, or parts of or additions to sites, for school buildings, including library buildings, structures, athletic fields, playgrounds, or other facilities.
- Purchasing school buses.
- Acquiring, installing, or equipping or re-equipping school buildings for technology.
- Refunding all or part of existing bonded indebtedness if the net present value of the principal and interest to be paid on the refunding bonds, excluding the cost of issuance, will be less than the net present value of the principal and interest to be paid on the bonds being refunded, as calculated using a method approved by the Department of Treasury.
- Accomplishing a combination of the above purposes.[25]

Such a bill would encourage more school districts to seek voter approval of sinking funds, "and thus increase property taxes for residents approving these proposals"[26] and further erode the tax limitations adopted under Proposal A of 1994.

OTHER PROPOSED CHANGES

Several other bills dealing with school finance have been introduced by Michigan legislators in the last year. Among these bills are House Bill 4917, House Bill 4582, and Senate Bill 688. See Table 2, "Other Proposed School Tax Changes," on page 14 for more information.

24. Section 1351a governs debt millage.

25. Revised School Code, 1976 PA 451, section 1351a.

26. Senate Fiscal Agency analysis of HB 4825.

TABLE 2. Other Proposed School Tax Changes

Bill No.	Bill Amending	Implications
HB 4917	1976 PA 451, section 1212	Would allow districts to levy additional millages under section 1211 to enhance operating revenues to levels of up to 2 times the State's per pupil allowance.
HB 4582	1976 PA 451	With voter approval, districts could levy up to 5 mills to create sinking funds to be used for real estate purchase, building construction or repair, or to "participate in paying for infrastructure improvements on public property or a public easement that directly impacts the use of school property..."
SB 688	1976 PA 451, section 1212	Would allow school districts to ask voter approval to levy up to 5 mills to create sinking funds for real estate purchase, construction, repair, and any other purpose allowed under 1351A.

Source: Anderson Economic Group analysis of relevant bills.

In addition to these statutory changes, a statewide bond issue has been proposed, which would create a fund—supported by state taxes—that would subsidize projects financed by the taxpayers of individual school districts. If approved by the voters of the state, and fulfilling its stated goal of encouraging and partially financing projects approved by the voters of local school districts, this would result in higher state taxes and higher local taxes.

While we have not projected the fiscal impact for these other proposals, the higher-millage scenario presented above for an expansion of "sinking fund" taxes alone provides an indication of the additional taxes that would arise from combining more than one legislative tax increase. See Table 1 on page 3.

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Fiscal Impact Methodology

The tax projections included in this report are based on specific assumptions about current taxable value, growth rates for taxable value, millages authorized under current and proposed laws, and voter behavior when confronted with future millage proposals.

COMPOSITION OF MILLAGE AND DISTRICTS

The total revenue impact of future tax changes is largely determined by the total number of mills levied, rather than the composition of those mills. Therefore, a scenario that incorporates an assumption of 5 additional mills being levied in 50% of the districts would accurately predict the revenue impact of 5 building & site mills and no other new millage, 2.5 building & site mills and 2.5 debt mills, as well as 5 sinking fund mills and no other additional millage.

We describe the various scenarios partially by the share of districts that adopt certain millages. Of course, some districts have much larger tax bases than others, and therefore would generate more tax revenue. A scenario based on adoption of a certain millage rate by "50% of the districts" would be more accurately described as "districts having 50% of the state's taxable value."

MILLAGE SCENARIOS

The least predictable of these variables is voter behavior. Therefore, we have provided a set of scenarios that cover the range of likely responses by voters to changes in law. Each scenario is reasonably conservative in assuming that changes occur gradually over a 10-year period.

To assess the impact of the proposed changes, a model was developed to simulate three millage growth scenarios. Each scenario assumes Senate and Executive approval of HB 4824, allowing districts to seek voter approval of "sinking fund" millages of up to 5 mills, and then spend the resultant revenue on purposes other than retiring debt. Our base scenario assumes an average increase of 2.5 mills, phased in over 10 years. Scenario two assumes an average increase of 1.5 mills, and scenario three assumes a 3.5 mill increase.

TECHNICAL ASSUMPTIONS

We assume that 62% of the debt, sinking fund, and building & site millage is paid by residential taxpayers, and the remaining by businesses (including farms). This is based on the current-law provision that does not exempt homestead property from these millages, and from the share of total taxable value accounted for by residential real property.[27]

"Fiscal Impact Simulation Results" on page 16 describes the results of our simulations. In addition, see Table 3 on page 17, and Table 4 on page 18, for more detail on the simulation results and assumptions.

27. Residential real property accounted for $114 billion of the $182 billion in statewide taxable value in 1995. While this ratio may have changed slightly, we have kept this a constant in our model. Source data: Michigan Department of Treasury, *The Michigan Real and Personal Property Tax*, March 1997, exhibit 8.

Fiscal Impact Simulation Results

The following summarizes the results of our simulations of an expanded school "sinking fund" tax:

BASE SCENARIO: 2.5 MILL INCREASE

Our base scenario assumes that "sinking fund" taxes grow at the same rate as debt, sinking fund, and building & site millage grew after the 1994 law expanded the allowable purposes for debt millage. Under this assumption, which implies an increase of 2.5 mills over ten years, an additional $5.43 billion will be collected from Michigan taxpayers from 2003 through 2013.[28]

Residential taxpayers will foot $3.37 billion of the total new taxes, and business and other non-resident tax sources will pay the remaining $2.06 billion. Table 3, "Michigan School Finance Simulation Results," on page 17 shows the impact in each of the ten years.

SCENARIO TWO: 1.5 MILL INCREASE

Our conservative estimate, scenario two assumes that the average statewide increase in sinking fund taxes will be 1.5 mills. Under this assumption, an additional $3.26 billion in property taxes will be collected from 2003-2013. We project that $2.02 billion of this amount will come from residential taxpayers, and $1.24 billion will come from non-resident tax sources. See Table 3, "Michigan School Finance Simulation Results," on page 17 for more detail on the impact.

SCENARIO THREE: 3.5 MILL INCREASE

Our more liberal estimate, scenario three assumes an 3.5 mill average tax increase over ten years.

Under this assumption, $7.60 billion in additional taxes will be collected over a ten-year period, of which $4.71 billion will be collected from residential taxpayers, and $2.89 billion from non-residential sources. For more detail, see Table 3, "Michigan School Finance Simulation Results," on page 17.

28. As indicated in the table, a 2.5 mill increase over ten years means an 0.25 mill increase in the first year of the ten-year period, which is 2004, an 0.50 mill increase in 2005, leading eventually to a 2.5 mill increase in 2013. Each of the scenarios uses a similar ten-year straight-line implementation schedule.

Table 3. Michigan School Finance Simulation Model Results

Base Scenario: 2.5 Mills Average Increase

	Cumulative Millage Increase	Annual Property Tax Increases (in billions)	Residential Burden Increase (in billions)	Non-Residential Burden Increase (in billions)
2003	0.00	$ -	$ -	$ -
2004	0.25	$ 0.07	$ 0.05	$ 0.03
2005	0.50	$ 0.15	$ 0.10	$ 0.06
2006	0.75	$ 0.24	$ 0.15	$ 0.09
2007	1.00	$ 0.34	$ 0.21	$ 0.13
2008	1.25	$ 0.44	$ 0.28	$ 0.17
2009	1.50	$ 0.56	$ 0.35	$ 0.21
2010	1.75	$ 0.69	$ 0.43	$ 0.26
2011	2.00	$ 0.82	$ 0.51	$ 0.31
2012	2.25	$ 0.97	$ 0.60	$ 0.37
2013	2.50	$ 1.13	$ 0.70	$ 0.43
SUM		**$ 5.43**	**$ 3.37**	**$ 2.06**

Scenario 2: 1.5 Mills Average Increase

	Cumulative Millage Increase	Annual Property Tax Increases (in billions)	Residential Burden Increase (in billions)	Non-Residential Burden Increase (in billions)
2003	0.00	$ -	$ -	$ -
2004	0.15	$ 0.04	$ 0.03	$ 0.02
2005	0.30	$ 0.09	$ 0.06	$ 0.04
2006	0.45	$ 0.15	$ 0.09	$ 0.06
2007	0.60	$ 0.20	$ 0.13	$ 0.08
2008	0.75	$ 0.27	$ 0.17	$ 0.10
2009	0.90	$ 0.34	$ 0.21	$ 0.13
2010	1.05	$ 0.41	$ 0.26	$ 0.16
2011	1.20	$ 0.49	$ 0.31	$ 0.19
2012	1.35	$ 0.58	$ 0.36	$ 0.22
2013	1.50	$ 0.68	$ 0.42	$ 0.26
SUM		**$ 3.26**	**$ 2.02**	**$ 1.24**

Scenario 3: 3.5 Mills Average Increase

	Cumulative Millage Increase	Annual Property Tax Increases (in billions)	Residential Burden Increase (in billions)	Non-Residential Burden Increase (in billions)
2003	0.00	$ -	$ -	$ -
2004	0.35	$ 0.10	$ 0.06	$ 0.04
2005	0.70	$ 0.22	$ 0.13	$ 0.08
2006	1.05	$ 0.34	$ 0.21	$ 0.13
2007	1.40	$ 0.47	$ 0.29	$ 0.18
2008	1.75	$ 0.62	$ 0.39	$ 0.24
2009	2.10	$ 0.78	$ 0.49	$ 0.30
2010	2.45	$ 0.96	$ 0.60	$ 0.37
2011	2.80	$ 1.15	$ 0.71	$ 0.44
2012	3.15	$ 1.36	$ 0.84	$ 0.52
2013	3.50	$ 1.59	$ 0.98	$ 0.60
SUM		**$ 7.60**	**$ 4.71**	**$ 2.89**

Source: Anderson Economic Group

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Table 4. School Finance Model Data

Millage Growth Scenarios

Variable Name	*Variables*	*Units*	*Values*
Tax Related Variables			
Statewide_TV	*Statewide Taxable Value of Property*	$billions, 2000	$ 241
TV_growth	*Taxable Value annual growth rate*	%	5
Res	*Residential Property with Homestead Exemption (as portion of total taxable value)*		0.62
BSM	*BSM millage authorization*	mills	-
debt	*Debt millage authorization*	mills	-
SF_1	*Sinking Fund millage authorization (low case)*	mills	1.5
SF_2	*Sinking Fund millage authorization (base case)*	mills	2.5
SF_3	*Sinking Fund millage authorization (high case)*	mills	3.5
Portion of School Districts Levying Selected Millage (at end of forecast period) -- Different Scenarios			
BSM_app	*BSM Apportionment - portion of school districts levying by end of forecast period*		100%
debt_app	*debt Apportionment*		100%
SF_app	*SF Apportionment*		100%
Simulation Parameters			
Tstart	*Model Start Time (year)*		2,003
Tstop	*Model Stop Time (year)*		2,013
Tstep	*Model Increments*		1

Implementation Schedule

Years>	Schedule>
2003	0%
2004	10%
2005	20%
2006	30%
2007	40%
2008	50%
2009	60%
2010	70%
2011	80%
2012	90%
2013	100%

Source: Anderson Economic Group

Policy Alternatives

There are alternatives to the proposed expansion of sinking fund taxing authority. These alternatives include:

RETAIN PROPOSAL A

Proposal A has been an unqualified success at its key objectives: reducing local school property taxes, increasing funding for schools, and reducing the difference between the highest- and lowest-spending school districts.

The first alternative, therefore, is to retain the current statutory tax limits protected by the Constitutional provisions established by Proposal A.

CONSIDER REGIONAL TAXES

Current law already provides for school districts to join together in asking voters to increase local taxes to augment spending for operating purposes. The law allows for up to 3 mills of taxing authority, on an intermediate school district-wide basis.

If the voters agree that more money is necessary, and that additional funds need to be expended for operating purposes, this option is already available.

PROHIBIT "DOUBLE DIPPING"

Current law allows for school districts to support true capital expenditures through debt millage, or sinking fund millage. Taxpayers rightly are concerned that levying both debt and sinking fund millage would be "double dipping" for capital purposes, since these are different ways of financing the same type of expenditure.

To prevent this, the legislature could amend the school code to prohibit school districts from levying any new "sinking fund" millage until outstanding debt obligations were retired or defeased.[29] It could similarly prohibit any new debt millage when a sinking fund millage was also levied.

TIGHTEN ALLOWABLE PURPOSES FOR DEBT MILLAGE

Another common-sense reform would be to tighten the allowable purposes for which "debt" millage could be expended. As indicated in "Bond, Building & Site, and Sinking Fund Millage" on page 10, the current statute allows "debt" millage to be used to fund certain operating expenditures. Taxpayers should be wary of voting upon themselves taxes to be repaid over the next ten or twenty years, when the money is used to buy services, maintenance, or short-lived assets like school buses—let alone undefined concepts such as "technology."

Such a reform would not only improve fiscal prudence, it would also increase the confidence voters would have in future debt millage proposals.

29. "Defeasing" the debt would be accomplished by purchasing US Government obligations or other very safe investments, in amounts sufficient to repay the debt, and putting them in a separate, segregated account. This is the traditional purpose of a "sinking fund."

EXPAND CHARTER SCHOOLS

Public school academies, commonly known as "charter schools," are public schools that operate under a charter from a public body. Such schools receive a per-pupil allowance for operating purposes.

Unlike traditional school districts, however, charter schools have no independent taxing authority, and cannot levy debt, sinking fund, or building & site millage. Therefore, they are forced to support both operating and capital expenditures within the per-pupil operating amount.

If state law is changed to effectively create an additional source of operating funds—by expanding the uses of "sinking fund" or other taxes—it would have the additional effect of increasing the existing disparity in funding between public school academies and traditional public school districts.

Overall enrollment within the public school system in the state has been relatively stable, and has grown much more slowly than funding.[30] However, in some areas of the state declining or expanding enrollment can challenge existing school districts.[31] Should such school districts find it difficult to handle the demands on their facilities within their per-pupil operating funds and their capital funds, they could encourage charter schools to educate a portion of the students in the area. The lower total per-pupil expenditures in charter schools would mean a larger amount of per-pupil capital funds available to the traditional public school district.

INSIST ON BETTER MANAGEMENT

The need for school districts to properly manage their funds is often overlooked in discussions of capital expenditures. In a properly managed school district, like a properly-managed household or business, maintenance and other needed expenditures are made out of current revenue. Painting, maintaining roofs and siding, occasional remodeling and refurnishing, and other such expenditures are commonly supported by household and business budgets. A well-managed school district will do the same.

It is difficult to legislate a concept such as "good fiscal management." However, the legislature and the state superintendant of schools should consider ways to encourage, or require, that school districts allocate an appropriate amount of their operating revenue each year to the repair, maintenance, and refurbishing of their existing school buildings. This would prevent "crises" occurring due to the lack of repairs or other poor management practices in the past.

School districts should also consider management practices that improve the efficiency of their non-instructional expenditures. Practices proven to save money

30. See Figure 5, "School Operating Revenue vs. Enrollment," on page 7.

31. Because the state guarantees funding on a per-pupil basis, schools with declining or increasing enrollment receive operating funds that closely match their enrollment changes. However, facilities cannot be erected or sold rapidly, so districts with unexpected, significant changes in enrollment do face additional costs related to either more facilities than needed, or the need for new facilities.

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include competitively bidding health care insurance; and outsourcing services such as janitorial, transportation, and maintenance.

About the Michigan Chamber Foundation

The Michigan Chamber Foundation is the sponsor of this study and subsequent report. The Foundation serves a number of purposes, including:

- To plan and conduct nonpartisan public education programs regarding free enterprise, productivity and basic economic issues affecting the State of Michigan.
- To conduct nonpartisan research and distribute policy studies on issues facing Michigan including, but not limited to, taxation, government regulation, health care, hazardous waste, crime, tourism and recreation, welfare, government spending and transportation.
- To engage exclusively in activities for charitable, scientific, educational, and other purposes as defined in section 501(c)(3) of the Internal Revenue Code.

The Foundation believes that the findings of the study are critical, and will help policy makers and Legislative leaders make well-informed decisions and create sound policy.

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Project Team

The principal author of this study is Patrick L. Anderson, Managing Director of Anderson Economic Group. He was assisted by Scott D. Watkins, Analyst; and Ilhan Geckil, Economist. Their backgrounds are summarized below.

PATRICK L. ANDERSON

Mr. Anderson is the Founder and Managing Director of Anderson Economic Group, and a principal in the BBK firm. He supervises the public policy and economics consulting practice of the firm, and has successfully directed projects with a wide range of state and local governments, nonprofit organizations, and private corporations.

Prior to founding Anderson Economic Group, Mr. Anderson served as the chief of staff of the Michigan Department of State, and as a deputy director of the Michigan Department of Management and Budget. Prior to his involvement in State Government, Mr. Anderson was an assistant vice president of Alexander Hamilton Life Insurance, where he shared responsibility for $5 billion in invested assets, and was an economist for Manufacturers National Bank of Detroit.

Mr. Anderson has written extensively on a number of topics involving economics and public policy. He has had over eighty-five articles published in periodicals such as *The Wall Street Journal, The Detroit News, The Detroit Free Press, American Outlook, Crain's Detroit Business*; and monographs published by the Mackinac Center for Public Policy, The Economic Enterprise Foundation of Detroit, the Ethan Allen Institute in Vermont, and the Heartland Institute of Chicago.

Mr. Anderson is a graduate of the University of Michigan, where he earned a Masters degree in Public Policy and a Bachelors degree in Political Science. He is an Adjunct Fellow with the Hudson Institute, and a member of the National Association for Business Economics.

SCOTT D. WATKINS

Mr. Watkins is an Analyst with Anderson Economic Group. He has extensive background in performing technical and policy research, creating market reports, and analyzing market and demographic data. Prior to joining the firm, Mr. Watkins was an Analyst in the automotive market and planning group at J.D. Power and Associates, where he contributed to research and analysis for clients including General Motors Corporation, Ford Motor Company, DaimlerChrysler Corporation, Bosch, and Johnson Controls. Mr. Watkins also held a marketing assistantship with Foster, Swift, Collins, and Smith P.C.

Mr. Watkins is a graduate of Michigan State University with a B.A. in Marketing from Eli Broad College of Business and a B.A. in International Relations from the James Madison College.

ILHAN K. GECKIL

Mr. Geckil is a Consultant with Anderson Economic Group, with expertise in economic and fiscal modeling, and advanced statistical & econometric analysis. Prior to joining the firm, Mr. Geckil served as an assistant consultant for the Project Development and Financial Consulting Corporation in Istanbul, Turkey; as an intern with Arthur Andersen, Istanbul, Turkey; and as a research assistant at Michigan State University.

Mr. Geckil holds a Masters degree in Economics from the Eli Broad Graduate School of Management at Michigan State University, and Bachelor degrees in Economics and International Relations from KOC University in Istanbul, Turkey. He is a member of National Association for Business Economics, and Strategy Forum.

STATE PROPOSAL

SPECIAL ELECTION - MARCH 15, 1994

PROPOSAL A

A PROPOSAL TO INCREASE THE STATE SALES AND USE TAX RATES FROM 4% TO 6%, LIMIT ANNUAL INCREASES IN PROPERTY TAX ASSESSMENTS, EXEMPT SCHOOL OPERATING MILLAGES FROM UNIFORM TAXATION REQUIREMENT AND REQUIRE 3/4 VOTE OF LEGISLATURE TO EXCEED STATUTORILY ESTABLISHED SCHOOL OPERATING MILLAGE RATES

The proposed constitutional amendment would:

1) Limit annual assessment increase for each property parcel to 5% or inflation rate, whichever is less. When property is sold or transferred, adjust assessment to current value.

2) Increase the sales/use tax. Dedicate additional revenue to schools.

3) Exempt school operating millages from uniform taxation requirement.

4) Require 3/4 vote of legislature to exceed school operating millage rates.

5) Activate laws raising additional school revenues through taxation including partial restoration of property tax.

6) Nullify alternative laws raising school revenues through taxation including an increase in income tax, personal tax exemption increase and partial restoration of property taxes.

Should this proposal be adopted?

Yes ☐
No ☐

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STATE OF MICHIGAN

JOHN ENGLER, Governor

DEPARTMENT OF MANAGEMENT & BUDGET

P.O. BOX 30026, LANSING, MICHIGAN 48909

PATRICIA A. WOODWORTH, Director

March 2, 1994

MEMORANDUM

TO: Governor John Engler

FROM: Patrick L. Anderson
Nick Khouri

SUBJECT: The Property Tax Limitations Protected by Proposal A

Under Proposal A, Article IX, Section 3 of the Michigan Constitution would be amended to read:

> *A law that increases the statutory limits in effect as of February 1, 1994 on the maximum amount of ad valorem property taxes that may be levied for school district operating purposes requires the approval of 3/4 of the members elected to and serving in the Senate and in the House of Representatives.*

Given our experience with the "Headlee" amendment, enforcing this provision will be easier if these limits are identified and publicized before the date of the election. Therefore, we have researched those laws in effect on February 1, 1994 that limit the "maximum amount of ad valorem property taxes that may be levied for school district operating purposes" and identify them below. These fall into two broad categories: school millage limits (including the definitions of "operating" and exceptions to "operating"), and general property tax limits which apply to schools. A table provides a quick reference summary of these limits.

We also identify laws which do not fit this description, and address other related questions.

Quick Reference on Tax Limits Protected by Proposal "A"

The following table outlines, for quick reference, the laws in effect on February 1, 1994 which would be constitutionally protected if proposal "A" passes.

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Limit Applies To:	*Limit:*	*Statute Protected:*
School Districts	6 mills on all property not exempt.	State Education Tax Act, Sec. 3.
School Districts	18 mills on all property, except homesteads.	School Code, Sec. 1211(1).
School Districts (1994-1996) Intermediate School Districts (1997 and after)	Enhancement mills limited to 3.	School Code, Sec. 1211c, 705.
Qualifying School Districts (Those spending above $6,500 per pupil in FY 94-95)	Mills necessary to "hold harmless" total spending in successive year; limited to qualified districts; limited to number of mills necessary in 1994; certified for each district by Department of Treasury.	School Code, Sec. 1211(3), 1211a.
School Districts	Prohibited from levying "allocated" mills.	School Code, Sec. 1211(7); Property Tax Limitation Act.
School Districts	Definition of "operating purposes;" Exceptions to "operating purposes" (Building and Site sinking fund, operating deficit, community college, libraries)	School Code, Sec. 260, 1211(8), 1212, 1351a, 1356(4), 1451; Act 261 of 1913 (Libraries).
Intermediate School Districts	For operation, special education, and vocational-technical education purposes, those mills allocated or levied in 1993 for each purpose.	School Code, Sec. 624a, 681a, 1727a.
Local Units of Government	Definition of "homestead," exemptions from property tax.	School Code, Sec. 1211(8); Public Utility Assessment Act.
Local Units of Government	"Truth in Taxation" notice, hearing, and separate vote requirements.	"Truth in Taxation," General Property Tax Act, Sec. 24e.
Local Units of Government	"Headlee" rollback requirements, formula for rollback, limit on number of annual elections, allowed ballot language, prohibition on "rollups."	General Property Tax Act, Sec. 34d.

millage rate, prescribe the formula for reducing the maximum authorized millage rate when assessed valuations grow faster than the rate of inflation ("Headlee rollbacks") and prohibit increases in the maximum authorized rate without voter approval ("Headlee rollups"). Municipalities could continue to levy less than their maximum authorized rate, and subsequently increase those rates up to the maximum authorized rate without additional voter approval, subject to Truth in Taxation.
Sec. 34d of the General Property Tax Act, Act 206 of 1893 (MCL 211.34d).

Limits Not Given Constitutional Protection

There are also, of course, many property tax limits and other laws concerning property taxes that would not be given the constitutional protection of a supermajority requirement for change. These include:

- Limits on units of local governments other than school districts, including cities, townships, counties, and villages. The phrase "school district" in the constitutional amendment clearly includes intermediate school districts.
- True general obligation debt for true capital investment. Such debt must be approved by the electors under Article IX section 6 of the Constitution, and must be used for the capital purposes allowed under the School Code in effect on February 1, 1994.
- Laws establishing and limiting TIFA's, DDA's, and Enterprise Zones, as long as such laws allow for the capture of tax revenue or its reimbursement, and a change in such laws would not allow an increase in the amount of taxes levied by school districts.
- Laws providing for true special assessments by units of local government, as defined and limited by our Supreme Court in *Kadzban v City of Grandville* 442 Mich 495 (June 1993) and *Dixon Road Group v City of Novi* 426 Mich 390 (November 1986) to assessments for physical improvements providing an proportional increase in the value of the property. Changes in laws allowing for special assessments to fund operating expenditures of school districts would require a supermajority vote, as well as possibly violating other constitutional provisions.
- Laws establishing the income tax credits based on property taxes paid ("homestead" or "circuit breaker" credits).

Changes Not Increasing Maximum Tax Revenue

Article IX section 3, if approved by the voters, would be read consistently with Article IX, section 31, which states general limitations on local property taxes and property taxes in general. Article IX, section 31 states in part:

> *If the definition of the base of an existing tax is broadened, the maximum authorized rate of taxation on the new base in each unit of Local Government shall be reduced to yield the same estimated gross revenue as on the prior base.*

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did not allow operating revenue (as defined on February 1, 1994) to be raised through any of these methods.
Sec. 260, 1211(8), 1212, 1351a, 1356(4), 1451 of PA 451 of 1976, as amended by PA 312 of 1993, and Act 261 of 1913 (for libraries; MCL 397.261 to 397.262.)

- The School Code requires the state department of treasury to certify in 1994 the millage allowed to be levied by each school district, other than the "enhancement" mills uniformly subject to a 3-mill limit. Although the School Code does not require this, we recommend that the department certify at the same time the number of mills allowed to be levied by each intermediate school district under Sections 624a and 681a.
  Sec. 1211a of PA 451 of 1976, as amended by PA 312 of 1993.

- The School Code would limit Intermediate School District mills to the 1993 allocation for operating mills, and the 1993 levies for vocational-technical education and special education purposes.
  Sec. 624a (operating), 681a (vocational-technical education), and 1727a (special education); and Sec. 681 to 690 and 1722 to 1729 (definition of voc-ed and special-ed purposes) of PA 451 of 1976, as amended by PA 312 of 1993.

General Property Tax Limitations

In addition to specific millage limits, the constitution would also protect those laws that otherwise limited the "maximum amount of ad valorem property taxes that may be levied for school district operating purposes." These include the following:

- The "Truth in Taxation" law would require the advance notice, standard disclosure, and separate board action now required for increases in the amount of operating property taxes that could be levied by a school district. For example, eliminating the requirement for a separate vote of the school board to levy taxes in excess of the prior year, or eliminating the disclosure or public notice provisions, would require a 3/4 vote of the legislature, under the proposed constitutional amendment. Changing the exact nature of the process by which that vote is taken, however, would not require a super-majority vote unless it allowed more taxes to be collected in the absence of some action by the voters or the elected board.
  Sec. 24e of the General Property Tax Act, Act 206 of 1893 (MCL 211.24e).

- The Property Tax Limitation Act provides the general implementation of Article IX, section 6 of the Constitution, which limits the total amount of property taxes levied by all units of local government. The first paragraph of Article IX section 6 specifically limits the taxes levied by school districts. Although the School Code would prohibit school districts from levying "allocated" mills under the 15-18 mill limit established by this section of the Constitution, the remainder of the Act could not be changed in any manner that would allow school districts to levy more property taxes without a supermajority vote of the legislature. Property Tax Limitation Act, Act 62 of 1933, (MCL 211.201 - 211.217a).

- The General Property Tax Act as amended by 1993 PA 145 (SB 1) would require specific wording on ballots asking for an increase in the maximum authorized

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All of the following mills would be subject to the supermajority vote requirement of Article IX, section 3, if Proposal A is approved by the voters on March 15.

- The State Education Tax Act would limit to 6 mills property taxes levied by the state on all property not exempt from property taxes under the Public Utility Assessment Act, PA 282 of 1905 (MCL 207.1 to 207.21). This tax would be levied on homesteads as well as other property not exempt from tax.
  Sec. 3 of PA 331 of 1993.

- The school code would limit school operating property taxes to 18 mills, with an exemption provided for principal residences.
  Sec. 1211(1) of PA 451 of 1976, as amended by PA 312 of 1993.

- The School Code would limit "enhancement" mills levied by school districts to 3 mills in 1994 through 1996, with their authorization ending thereafter.
  Sec. 1211c of PA 451 of 1976, as amended by PA 312 of 1994.

- The School Code would allow "enhancement" mills to be levied by an Intermediate School District, and limit the number of mills to 3, beginning in 1997.
  Sec. 705 of PA 451 of 1976, as amended by PA 312 of 1993.

- The School Code would limit the additional "hold harmless" millage levied by school districts which had per-pupil revenue in excess of $6,500 in FY1994-95. Only those districts qualifying in 1994 could levy mills under this section, and only for the purposes stated.
  Sec. 1211(3) of PA 451 of 1976, as amended by PA 312 of 1993.

- The School Code would prohibit levying "allocated" mills under the Property Tax Limitation Act, PA 62 of 1933 (MCL 211.201 to 211.217a).
  Sec. 1211(7) of PA 451 of 1976, as amended by PA 312 of 1993.

- "Homestead" would be defined in the School Code, and the general exemptions to property taxes would be defined in the Public Utilities Assessment Act. These could not be changed to allow *more* property taxes to be levied by schools without a supermajority vote of the legislature. (These Acts could be changed to allow *less* property taxes to be levied; bills currently introduced to expand the definition of "homestead" for this purpose would not require a 3/4 vote.)
  Sec. 1211(8) of PA 451 of 1976, as amended by PA 312 of 1993; Act 282 of 1905 (MCL 207.1 to 207.21).

- The School Code's definitions of "operating" purposes and the exceptions to operating purposes could not be changed from the definitions in effect on February 1, 1994 without a supermajority vote, if such a change allowed more operating property taxes to be levied by school districts. The provisions governing the exceptions to "operating," (sinking funds for building and site acquisition and construction, taxes levied to eliminate an operating deficit, taxes levied for the operation of a community college, and pass-through revenue to libraries), could be changed without a supermajority vote, as long as the changes

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This states a general principle that could be used to allow changes in the definitions of exemptions, or other changes involved in setting the limits, which would not require a supermajority vote and would comply with the Constitutional provision establishing special protection for school operating property tax limits. A change in a definition of the base of the tax, such as a change in the definition of the "homestead" exemption, could take place without a supermajority vote, if the maximum authorized rate was reduced so that the "statutory limits in effect as of February 1, 1994 on the maximum amount of ad valorem property taxes that may be levied for school district operating purposes" would not be increased.

Thus, the legislature could tighten the general law exemptions from property taxes, so long as it was treated as an expansion in the base of a tax and caused a reduction in the maximum authorized rate of taxation, and therefore the maximum property tax revenue was not increased. Of course, a change in a law that resulted in an expansion of the property tax base, but was not accompanied by a "Headlee" reduction in the rate would require a supermajority vote.

cc: Patricia Woodworth
Doug Roberts
Madhu Anderson
Lucille Taylor
Dan Pero
Carol Viventi
Mark Murray

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STATE OF MICHIGAN
OFFICE OF THE GOVERNOR
LANSING

JOHN ENGLER
GOVERNOR

April 14, 1994

Michigan State Senate
State Capitol Building
Lansing, MI 48913

Dear Ladies and Gentlemen:

Today I have vetoed and am returning to you herewith, Enrolled Senate Bill 597.

The constitutional amendment adopted by the people of Michigan on March 15, 1994, limits property taxes for school operating purposes. It requires that any legislation to exceed that limit be approved by 3/4 of both the House and Senate. House Bill 597 clearly falls under this requirement and did not receive a 3/4 vote on its final passage in the House. Even though the constitutional amendment does not become effective until May 1, 1994, I made it clear in a letter to legislative leaders on March 17, 1994, that I felt we were "obligated to uphold the wishes of the citizens" on legislation enacted before May 1. This letter included a list of all the Public Acts covered by the 3/4 requirement. Section 1351a of the School Code, which Senate Bill 597 amends, is on this list. So, even if I found the content of the bill wholly acceptable, I would not sign it because it failed to get a 3/4 vote in both houses of the Legislature.

I do not, however, find the bill acceptable as a whole. For the most part, I supported the bill as it passed the Senate, permitting school districts to issue bonds to finance the furnishing of partially remodelled schools and the purchase of technological equipment for student instruction purposes.

In the House, language was added to Senate Bill 597 to allow districts to refund bonds at higher interest rates if these bonds were consolidated with a new debt issue. This is simply fiscally imprudent. In addition, the language requiring that the technology must be for hardware and for classroom instruction purposes was weakened. Lastly, the bill allows the use of sinking funds for the purchase of technology. I am not persuaded that this is an appropriate purpose for sinking funds.

I will support an amendment to the School Code that does allow bonding for furnishing of partially remodelled schools and for technological hardware for instructional purposes as long as language is included that ensures that the bonds for technology cannot be issued for longer that the useful life of the equipment. I am also supportive of the language in section 1262 of Senate Bill 597 which allows districts to enter into an installment service contract for computers and telephones. I have instructed the Department of Treasury to prepare draft legislation which reflects these changes. It will be delivered to the four legislative leaders tomorrow.

Proposal A promised Michigan homeowners permanent property tax relief -- guaranteed in the Constitution. That promise cannot and will not be broken.

Proposal A was a tremendous victory for Michigan taxpayers. We cannot stand by and let that historic step forward be reversed piecemeal by those who preferred the old school finance system – a system that was unfair to students and taxpayers alike. To allow such tampering would betray the trust of the citizens of our great state, and I will not stand for it.

For these reasons, I am returning Enrolled Senate Bill 597 without signature.

Sincerely,

John Engler
Governor

JE:jmc:klk
cc: Michigan House of Representatives
The Honorable Richard Austin

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